

Franchise Tax Board**ANALYSIS OF ORIGINAL BILL**

Author: Cedillo Analyst: Deborah Barrett Bill Number: SB 1146
Related Bills: See Legislative History Telephone: 845-4301 Introduced Date: February 4, 2008
Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: FTB Disclosure Reciprocal Agreement With City Or County/Delete Repeal Date & Allow Request For Any Other Information By Affidavit/City Or County Provide Business Tax Program Information To FTB

SUMMARY

This bill would do the following:

- Require a city or county that administers a business tax program to provide specific data to the Franchise Tax Board (FTB),
- Remove cost reimbursement requirements from the existing local government sharing program,
- Expand the local government sharing statutes to include counties, and
- Authorize a city or county and FTB to exchange tax data.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to make the local government sharing provisions permanent and take advantage of efficiencies in the exchange of data between a city and county and FTB.

EFFECTIVE/OPERATIVE DATE

This bill would be effective January 1, 2009. The provisions relating to city business tax reporting would be operative for a city or county that assesses a tax or requires a city or county business license on or after that date to the extent economically feasible, except that in no event may a city or county comply any later than December 31, 2009. The provisions related to FTB providing confidential tax data to cities and counties would be operative on January 1, 2009.

POSITION

Pending.

Board Position:

_____ S	_____ NA	_____ NP
_____ SA	_____ O	_____ NAR
_____ N	_____ OUA	_____ X PENDING

Department Director**Date**

Selvi Stanislaus

4/4/08

ANALYSIS

STATE LAW

FTB compiles information from many different sources including employers, financial institutions, and federal and state entities for purposes of assuring compliance with the state's income tax laws. When FTB receives information indicating that a tax return should be filed for a taxable year, but has no record of a return, FTB may contact the individual taxpayer to request that the taxpayer file a return or explain why no return is required. When a taxpayer is required to file a return, but fails to do so, FTB is authorized to assess tax based on estimated income from all available sources.

Existing state law prohibits the disclosure of any taxpayer returns and return information, except as specifically authorized by statute. Generally, disclosure is authorized to other state tax agencies, federal tax agencies, other state tax agencies, and the Multistate Tax Commission for tax administration purposes only. Tax officials of political subdivisions of the state may obtain tax information only upon affidavit. At the time the tax official requests the tax information, they must provide a copy of the affidavit to the taxpayer whose information is sought, and upon request, make the obtained information available to that person. Unauthorized disclosure of state tax returns and return information is a misdemeanor and improper disclosure of federal tax returns and return information is a felony.

FTB is authorized to provide limited specified tax return information to cities for the administration of local city business license requirements. The information is limited to only those taxpayers within the city jurisdiction and includes the following:

- Taxpayer Name,
- Taxpayer Address,
- Taxpayer Social Security Number or Taxpayer Identification Number, and
- Principal Business Activity Code

Information provided to the cities may be used by city employees only for city business tax purposes. FTB is required to execute an agreement with each participating city that, among other things, provides that the annual cost incurred by FTB to provide the city data is reimbursed by the city to FTB.

THIS BILL

This bill would move provisions from one section to another that allow tax officials of political subdivisions of the state to obtain otherwise confidential taxpayer information from FTB by affidavit. It appears the bill also would eliminate access to taxpayer information by use of an affidavit by entities currently covered as "political subdivisions," such as villages or townships.

This bill would expand the local governments that can receive FTB taxpayer information to include any county that administers a business tax. Information provided by FTB to a city or county could be used in the administration of a city or county business tax or as otherwise authorized by law.

This bill would remove the requirement that a city reimburse FTB for costs as a condition for FTB to disclose state income tax data to a city and would instead authorize a city or county to enter into a reciprocal agreement to exchange tax data between the city or county and FTB.

The bill would define reciprocal agreement to mean an agreement to exchange information for tax administration purposes between tax official of a city or county and taxing authorities of FTB.

The bill would remove the express authorization for FTB to disclose confidential tax information to cities

This bill would enact a new provision that would apply to a city or county that assesses a city or county business tax or requires a city or county business license. It would require information collected in the course of administering city or county business tax requirements to be furnish to FTB on an annual basis. The information that would be required would be limited to the following:

- Name of the business if a corporation, partnership, or limited liability company, or the owner's name if a sole proprietorship
- Business mailing address
- Federal employer identification number, if applicable, or the business owner's social security number
- Standard Industry Classification Code (SIC) or North American Industry Classification Code (commonly referred to as "NAICS")
- Business start date
- Business cease date
- City or county number
- Ownership type

This bill would require the information to be provided to FTB on magnetic media, such as tapes or compact discs, through a secure electronic process, or in other machine-readable form, according to standards prescribed in regulations issued by FTB. The cities and counties would begin providing information as soon as economically feasible, but no later than December 31, 2009. Use of the data would be limited to state tax enforcement or as otherwise authorized by law.

This bill would remove the repeal date of the provisions that authorize city access to state tax data.

IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

As written, the bill would remove FTB's discretionary authority to release state income tax data to the city or county. The language should be revised to restore FTB's express authorization to disclose confidential tax data to resolve any potential disclosure issues for the department.

Additionally, the current agreements executed between the cities and FTB under the local government sharing statute detail specific requirements for safeguarding the confidentiality of tax data in possession of the cities. As current law is permissive, FTB can cut off access to data by any city that fails to comply with the standards of care imposed under the agreement. Removing the permissive nature of the statute may interfere with FTB's ability to stop unauthorized disclosures in cases where a city or county fails to exercise due care in its handling of confidential tax information obtained from FTB.

While FTB expects the city business tax data would be extremely beneficial in its non-filing enforcement efforts, a study done by FTB found that county business tax data failed to yield a sufficient cost benefit ratio for purposes of FTB's non-filer programs. The low volume of available data and variance in county capability to provide data in the formats required were contributing factors that resulted in the low yield estimate.

The zip code used on a taxpayer's return is the primary indicator to identify taxpayers within specific city jurisdictions. As county level jurisdiction determined by zip code would overlap city jurisdiction determined in the same way, FTB is unable to distinguish under which jurisdiction (city or county) a taxpayer would fall. Sending the same taxpayer information to both a city and a county may lead to disputes between the city, the county, the taxpayer, and the department.

This bill would allow state income tax information to be used for city or county tax administration purposes or as otherwise authorized by law. Because local ordinances vary by city and county, FTB cannot control how a city or county would use the taxpayer information it would receive under this bill. It is recommended that the bill be revised to specify that the information may only be used as authorized by state or federal law to ensure legislative oversight of confidential tax data.

TECHNICAL CONSIDERATIONS

The following Technical Changes are recommended to correct grammatical errors in the language:

On Page 3, Line 21, after "and" delete "taxing authorities of". Franchise Tax Board and taxing authorities are the same entity in this sentence.

On Page 5, Line 30, after "Board", delete "with".

LEGISLATIVE HISTORY

SB 978 (Harman 2007) would require cities that assess a city business tax or require a city business license to report certain information annually to FTB. This bill was held in the Assembly Appropriations Committee.

SB 1373 (Cedillo, Stats 2006, Ch. 513) extended the repeal date of the local government sharing program to December 31, 2011.

AB 63 (Cedillo, Stats 2001, Ch. 915) authorizes the disclosure of tax information to cities provided a contract is executed that requires cities to reimburse FTB for costs incurred.

AB 1105 (Jackson, Stats. 1999, Ch. 67) repealed the requirement that cities maintaining a computerized record-keeping system or that have access to such a system annually furnish FTB with information regarding taxpayers who pay city business license taxes.

PROGRAM BACKGROUND

During fiscal years 1993 through 1999, California law required that each city maintaining a computerized record keeping system or that has access to such a system and that assesses a business license tax or fee annually furnish FTB a list of all businesses subject to tax in the preceding year. In 1999, this statute was repealed.

Acknowledging the historical revenue generating performance of city business tax data, as a part of its Tax Gap Strategies FTB requested and received funding to initiate a program to purchase city business tax 2005 and 2006 tax year data from local government agencies. Fifteen cities contracted with FTB for 2005 data at a cost of \$123,100 to provide lists of businesses in their jurisdictions that were assessed a tax or issued a license. Thirty-eight cities provided city business tax data for the 2006 tax year at a cost of \$167,000. The department anticipates that approximately \$1 million would be derived from this source of data each year.

FISCAL IMPACT

The provisions of this bill would result in approximately 480 cities and 58 counties providing files on an annual basis to FTB that would require additional staffing to coordinate the receipt of the files, establish secure electronic communication protocols with the cities and counties, and test the quality of the data for departmental use. Additionally, the current costs for collecting and distributing the tax data to the cities would no longer be reimbursed by the cities, but would still be incurred by FTB. These costs would be offset by the savings from no longer purchasing city business tax data. Costs will be developed as the bill moves through the legislative process.

ECONOMIC IMPACT

Based on data and assumptions discussed below, the PIT and Corporation Tax revenue impact from this bill would be as follows:

Revenue Analysis for SB 1146 – as introduced 2/4/08 Effective and Operative on 1/1/09 Assumes Enactment after 6/30/08 (\$ in Millions)			
Fiscal Year	2008-09	2009-10	2010-11
Mandatory Reporting	\$6	\$23	\$35

This analysis does not consider any possible changes in employment, personal income, or gross state product that could result from this bill.

Revenue Discussion

The revenue impact of this bill would be determined by the extent the mandatory annual transmittal of local business and licensing information by cities and counties statewide yields new income tax revenues due to greater non-filer detection and enforcement. The timing of the cash flow from the new revenue generated by this bill would not begin until fiscal year 2009-10. This assumes that cities and counties would begin mandatory reporting of local business activity as early as January 1, 2009. It is expected that this new information will result in new non-filer contacts, at first, that are associated with the 2008 tax year. The non-filer assessments will start to be sent in late 2009 or early 2010.

The revenue estimate was developed in the following steps:

- Started with actual revenue collected for a similar statewide program in effect during tax years 1994 through 1998 of \$27 million.
- Adjusted total by a factor of 197% to reflect growth in personal income and population from 1996 to 2007 resulting in \$52.5 million (\$27 million x 1.97);
- Applied a 10% gross-up adjustment to reflect data technology advancement by cities and counties over the last decade (more cities are able to produce the data required by FTB), resulting in \$57.5 million (\$52.5 million x 1.10);
- Increased estimated revenue impact by 3% to reflect county participation based on a recent internal feasibility study, resulting in \$59 million (\$57.5 million x 1.03);
- Reduced projected revenue to account for data currently received from cities voluntarily providing data, resulting in \$56.6 million (\$59 million - \$2.5 million);
- Adjusted first-year impact to account for the following assumptions:
 - 70% participation by cities in the first year (will grow to 100% by fourth year);
 - 80% of available records will be transmitted in time for annual processing;
- Determined the expected flow of revenue based on historical collection data.

Initially, the cash flow impact estimated for fiscal year 2009-10 would be limited to \$6 million in revenues gained. This amount is based on a projected 50,000 new contacts that result in potential collections of roughly \$600 per contact, or \$30 million in (50,000 contacts x \$600 tax = \$30 million). Given historical payment trends, it is anticipated that 20% of this money would be received by June 30, 2010. In the 2010-11 fiscal year, an additional 45% of revenue generated in the first year would be collected, roughly \$14 million. Combining both the initial flow of revenue associated with the 2009 tax year information, an estimated \$9 million, and the \$14 million estimated for the second year, the anticipated revenue would result in a total of \$23 million of revenue gain in 2010-11 (\$9 million + \$14 million)

It is expected that by the fifth year after enactment the direct revenue generated from these information sources will approximate \$50 million per year. There is likely to be an increase in voluntary compliance over the long run, but such indirect revenue gains were not considered in this analysis. While the cash flow impact from this proposal would begin to be realized in the 2009-10 fiscal year, the revenue gains for each fiscal year are accrued back one year. This is because the underlying tax liability for which the assessments would be based is attributed to a prior tax year.

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